

Appeal of James M. and Mabel H. Holmes

circumstances, respondent's notices of proposed assessment together with the schedules attached thereto are the best available secondary evidence of the contents of the returns as to the gross income and expenses reported.

Los Osos Vendors owned music machines, multiple-odd bingo pinball machines, flipper pinball machines and miscellaneous amusement machines. The equipment was placed in various locations, such as bars and restaurants. The proceeds from each machine, after exclusion of expenses claimed by the location owner in connection with the operation of the machine, were generally divided equally between Los Osos Vendors and the location owner. With respect to some of the miscellaneous amusement machines, Los Osos Vendors received a fixed sum each week rather than half of the net proceeds.

The gross income reported in tax returns of Los Osos Vendors was the total of amounts retained from locations. Respondent determined that Los Osos Vendors was renting space in the locations where its machines were placed and that all the coins deposited in the machines constituted gross income to it. Respondent also disallowed all expenses of Los Osos Vendors pursuant to section 17359 (now 17297) of the Revenue and Taxation Code which read:

In computing net income, no deductions shall be allowed to any taxpayer on any of his gross income derived from illegal activities as defined in Chapters 9, 10 or 10.5 of Title 9 of Part 1 of the Penal Code of California; nor shall any deductions be allowed to any taxpayer on any of his gross income derived from any other activities which tend to promote or to further, or are connected or associated with, such illegal activities.

Except with respect to those miscellaneous amusement machines placed in locations for a fixed weekly amount, the evidence indicates that the operating arrangements between Los Osos Vendors and each location owner were the same as those considered by us in Appeal of C. B. Hall, Sr., Cal. St. Bd. of Equal., Dec. 29, 1958, 2 CCH Cal. Tax Cas. Par. 201-197, 3 P-H State & Local Tax Serv. Cal. Par. 58145. Our conclusion in Hall that the machine owner and each location owner were engaged in a joint venture in the operation of these machines is, accordingly, applicable here.

In Appeal of Advance Automatic Sales Co., Cal. St. Bd. of Equal., Oct. 9, 1962, CCH Cal. Tax Rep. Par. 201-984, 2 P-H State & Local Tax Serv. Cal. Par. 13288, we held the ownership or possession of a pinball machine to be illegal under Penal Code sections 330b, 330.1 and 330.5 if the machine was predominantly a game of chance or if cash was paid to players for unplayed free games, and we also held bingo pinball machines to be predominantly games of chance.

It is clear from the testimony of a collector for Los Osos Vendors and the testimony of three location owners that cash was paid to players of the pinball machines for unplayed free games. Most of the pinball machines owned

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the protest of James M. and Mabel H. Holmes to proposed assessments of additional personal income tax in the amounts of \$1,190.48, \$6,929.35, \$9,477.75 and \$5,003.94 for the years 1951, 1952, 1953 and 1954, respectively, be modified in that the gross income is to be recomputed in accordance with the opinion of the board and penalties for failure to file returns are to be deleted. In all other respects the action of the Franchise Tax Board is sustained,,

Done at Sacramento, California, this 17th day of April, 1963, by the State Board of Equalization.

<u>Paul R. Leake</u>	, Acting Chairman
<u>Richard Nevin</u>	, Member
<u>Geo. R. Reilly</u>	, Member
<u>Alan Cranston</u>	, Member
<u> </u>	Member

ATTEST: Dixwell L. Pierce , Secretary